U S WEST, Inc.
Suite 700
1020 Nineteenth Street, NW
Washington, DC 20036
202 429-3106
FAX 202 296-5157

U S WEST

Cyndie Eby
Executive Director-
Federal Regulatory

EX PARTE

April 4, 1995

Mr. William F. Caton
Secretary
Federal Communications Commission
1919 M Street, NW, Room 222, SC-1770
Washington, DC 20554

RE: CC Docket 95-185 Interconnection Between LECs & CMRS

Dear Mr. Caton:

Today, U S WEST (USW) representatives met with Gregory L. Rosston, Deputy Chief Economist, Office of Plans and Policy to discuss its views relative to the above referenced proceeding. USW expressed the following points: 1) good faith negotiations have resulted in reasonable interconnection arrangements; 2) CMRS to wireline interconnection is intrastate in nature; 3) bill and keep is not economically rational; and 4) CMRS to wireline interconnection should be governed by the negotiation process provided for in Sections 251 and 252 of the Telecommunications Act of 1996. Details of the presentation are attached. A copy of *Wireless/Wireline Interconnection Arrangements - Rate Structures and Rate Comparisons Including Technical and Regulatory Considerations* was provided.

USW was represented by Professor Robert G. Harris, Law & Economics Consulting Group, Inc., Keith Galitz, Executive Director-Wireless Markets Group and Cyndie Eby, Executive Director, Federal Regulatory.

In accordance with Section 1.1206(a)(2) of the Commission's rules, the original and one copy of this letter are being filed with your office. Acknowledgment and date of receipt are requested. A duplicate of this letter is included for this purpose.

Sincerely,

Cyndie Eby

Attachments
cc: Gregory L. Rosston

CMRS-LEC Interconnection Pricing

Ex Parte Presentation to the FCC
Professor Robert G. Harris
on behalf of U S WEST Communications, Inc.

CC Docket No. 95-185
April 4, 1996

Presentation Overview

- Bill and Keep harms public interest objectives
- Many CMRS providers are large competitors negotiating from positions of economic strength
- Substantial differences exist between CMRS providers and LECs
- Guidelines for effective LEC-CMRS Interconnection

Bill and Keep is Not Economically Rational

- The cost of tandem switching and transport is neither zero nor trivial
- A price of zero leads to a "tragedy of the commons" and/or regulatory arbitrage:
  - Examples of traffic congestion on tandem switches
  - IXCs will have an incentive to terminate interLATA traffic through CMRS switches to avoid access charges

Bill and Keep Would Reduce Intrastate Revenue

- A federal bill and keep mandate would unfairly reduce LEC state revenues
- $70 million in intrastate revenue from CMRS interconnection supports U S WEST's residential customers
- According to CTIA, LECs received $800 million in intrastate revenue from CMRS interconnection in 1995

Bill and Keep Would Be a Regressive Tax

- CMRS use is positively correlated with income
- Pricing interconnection below cost is equivalent to a regressive tax paid by landline rate payers to CMRS providers and subscribers
- Landline state rate payers (essential service) should not be required to subsidize CMRS providers and subscribers (premium service)

Bill and Keep Would be a Windfall for PCS A&B Block Winners

- PCS license bids reflected the expected net present value of licenses, including interconnection costs
- Bill and keep increases the expected value of licenses by reducing costs, creating a windfall
- Windfall profits are at the US Treasury's expense
- "Interim" rules last longer than intended: the longer bill and keep lasts, the larger the windfall

Bill and Keep is Not Used in Other Industries

- Regulated Industries:
  - Railroads
  - Banking (SWIFT)
- Non-Regulated Industries

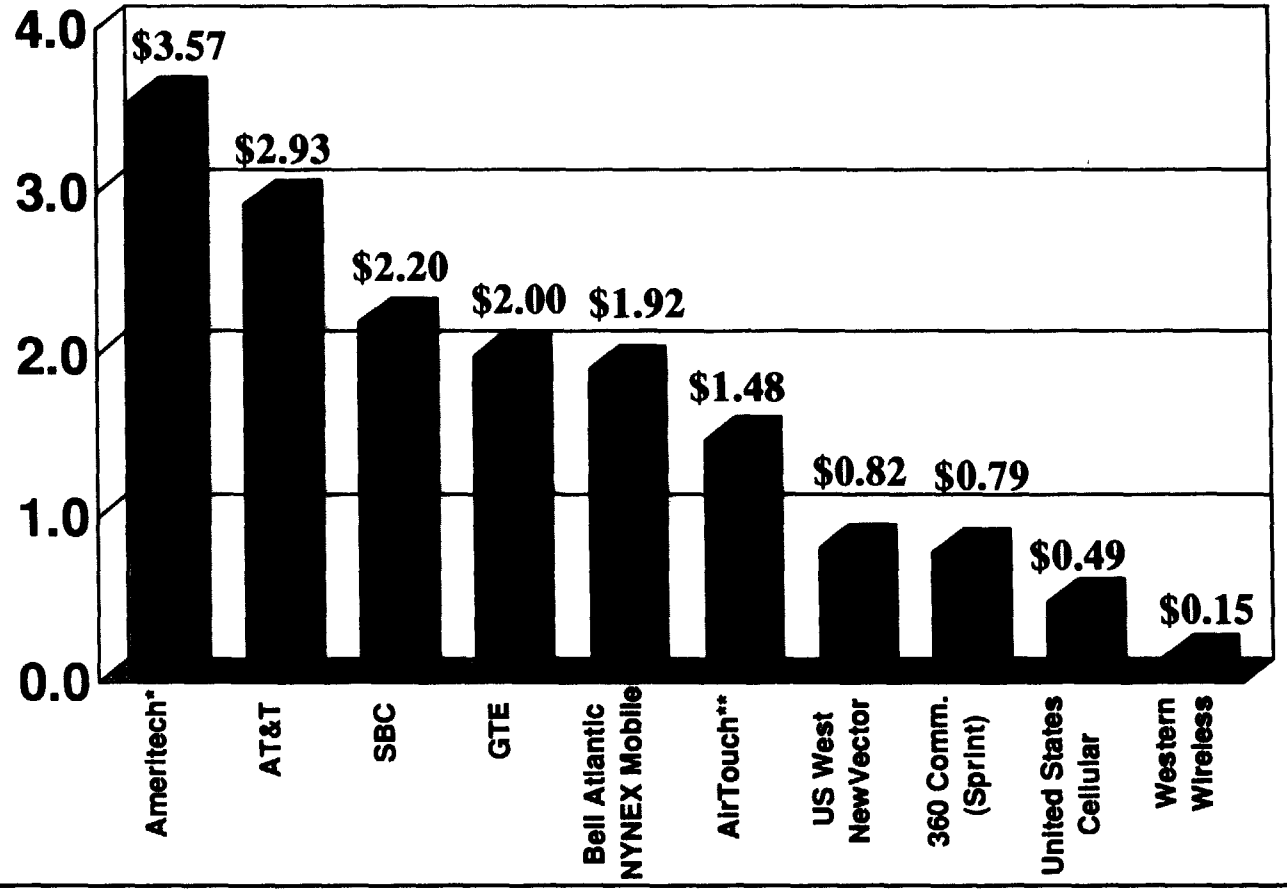
CMRS Providers Continue to Grow Dramatically

- December '94: 24.1 million subscribers
- March '96: 36.4 million subscribers and growing
- Anticipate a continuing 40% growth rate
- 1 new subscriber every 3 seconds
- 1995 revenues $19 billion; up 34% from $14.2 billion in 1994

Source: CTIA, Press Announcement, March 25, 1996

Large CMRS Providers Are Strong Negotiators

1995 Wireless Revenues
($Billions)



Notes:

*Includes Directory and other revenues.

**Domestic revenues only.

Source: Company Reports.

CMRS Bargaining Power is Strengthened by State Regulation of Interconnection Agreements

- U S WEST is required to file tariffs for paging and ESMRS interconnection in 9 of its 14 states, cellular in 3 states, and catalogues or contracts in the remaining states
- State regulators examine tariffs, catalogues, and contracts
- US WEST provides interconnection under the same terms to all wireless service providers
- CMRS providers who face discriminatory treatment can file complaints with state regulators

Factors Preventing CMRS Providers from Competing Directly with LECs

- 1FR is held below cost in most US WEST states
- CMRS usage is priced on a per minute basis for both originating and terminating calls
- CMRS transmission quality is not as high as LECs

Key Differences Between LECs and CMRS Providers

- LECs have carrier of last resort and universal service obligations
- Many LECs are required to price 1FR below cost at geographically averaged rates w/o usage charges
- LEC retail rates <u>are</u> regulated

- CMRS providers only serve profitable customers
- CMRS providers receive approximately 40 cents per minute for <u>incoming and outgoing</u> local usage
- CMRS retail rates <u>are not</u> regulated

Incremental Revenues Associated with Local Calls

(Rates are per MOU)

Type of Call	CMRS Revenue	Wireline Revenue	% of CMRS MOUs
CMRS to Wireline	44¢ (cellular usage fee)	2.3¢ (average CMRS interconnection rate)	70%
Wireline to CMRS	44¢ (cellular usage fee)	0*	25%
CMRS to CMRS	88¢ (2 x cellular usage fee)	0 (direct) 2.3¢ (via LEC)	5%

Wireline to Wireline:

- Local calls generate 0 (zero) usage revenue*
- Accounts for 93% of <u>all</u> local MOUs, not including calls originated by ILECs

**The vast majority of U S WEST's local wireline calls are carried on a flat rate basis.*

Guidelines for LEC-CMRS Interconnection

- Allow "good faith" privately negotiated agreements
- Set broad guidelines to prevent anticompetitive behavior
- Allow the flexibility to accommodate different LEC pricing agreements
- Only prohibit anticompetitive agreements

Costs and Pricing for LEC-CMRS Interconnection

- Interconnection prices should be based on the following cost categories:
  - incremental costs (TSLRIC)
  - joint and common costs

LEC-CMRS Interconnection Cost Estimates

Company	Cost Estimate	Network Elements	Cost Type
Vanguard	0.57¢ (peak)	Unspecified elements	Incremental from engineering study
USTA/SPR	1.3¢ (avg.)	Terminating end office switching	Incremental from econometric study
Cox (Brock), cited by FCC	0.2¢ (avg.)/ 2.1¢ (peak)	Originating and terminating end office switching; interoffice transport	Incremental from engineering study
Pac Tel	0.5-1.0¢ (avg.)/ 5¢ (peak)	Tandem and terminating end office switching; common transport	Incremental

Source: Company filings in this proceeding.

Comparison of Intrastate Long Distance Toll and CMRS Charges

Rates are per MOU during peak hours	IXC Intrastate Service	CMRS Service
Terminating switched access/ interconnection prices	4.4¢	2.3¢
End user retail prices	16.4¢	44¢
Terminating access/interconnection price as percent of end user retail prices	27%	3.6%

Source: PNR and Associates, 1995; MTA/EMCI 1994.

Flawed "Interim" Policies Should be Avoided

- Flawed interim policies:
  - create uncertainty in the marketplace
  - distort competition
  - create constituencies with a vested interest in their perpetuation
- Policies such as the ESP/ISP exemption from access charges lasted longer than intended

Initiate Interconnection and Access Proceedings

- Rebalance local rates
- Regulate functionally equivalent services under the same regime regardless of service user
- Use similar pricing structures for similar services to reduce regulatory arbitrage opportunities
- Allow existing agreements and negotiations to continue during the interim

Wireless/Wireline Interconnection Arrangements - Rate Structures And Rate Comparisons Including Technical And Regulatory Considerations

Prepared For: U S WEST Communications

Prepared By: Malarkey-Taylor Associates/
Economic Management and Consultants International

MTA
EMCI
Communications Consultants

January, 1996

Table Of Contents

1.0 Introduction

Presently, there are about 160 million telephone lines served by Local Exchange Carriers (LECs) in the United States. Total wireless services (cellular, paging, Specialized Mobile Radio, Personal Communication Services, etc.) collectively have about 70 million subscribers. But the total number of landline phones is over five times greater than the number of subscribers of the largest wireless service, which is cellular. Consequently, for any wireless service to have value and utility, access to the landline subscribers is absolutely essential.

Obtaining interconnection arrangements that are technically suitable has proven to be difficult until fairly recently. Dating back to 1949, most of the interconnection arrangements that are used by the wireless services are the result of regulatory action instead of voluntary offerings on the part of the LECs. Fortunately, this has changed in recent years. Indeed, in 1991 the industry began joint discussions on additional types of interconnection arrangements and agreements were reached in 1993 that resulted in several new types of interconnection. The technical aspects of the different interconnection arrangements are explained in Section 3.0 while the regulatory actions are detailed in Section 4.0.

But an even more daunting task has been negotiating an interconnection rate that is fair and equitable to both parties. Interconnections between LECs and Interexchange Carriers (ICs) are predominantly interstate in nature and thus regulated by the Federal Communications Commission (FCC). Although the rates differ for the LEC-IC interconnection, the rate structure is essentially the same for each company. Such is not the case with interconnection agreements between wireless carriers and the LECs. These